is simply irrelevant, unless it can be demonstrated that the identity of the called party *causes* the costs incurred in delivering the call to change (i.e. is a cost driver). No such demonstration has been made in this case.

Dr. Harris refers in his testimony to the possibility of an "outright subsidy" being requested by the CLECs and to the existence of a "current subsidy system." What his testimony fails to make clear is exactly who he asserts is subsidizing whom. It appears that Dr. Harris is asserting that SWBT would be subsidizing, through reciprocal compensation payments, the service provided by a CLEC to an ISP. As with any subsidy claim, there are two components. In this case, they would be: (1) is the service provided by CLECs to ISPs being subsidized?, and (2) would the payment reciprocal compensation for the delivery of calls to ISPs provide such a subsidy? In order for SWBT's claim to be validated, an affirmative response to each question is necessary. Of course, the first question is moot unless the answer to the second question is yes: as a factual matter, CLECs may or may not subsidize the service provided to ISPs by utilizing revenues from services provided to other customers. The potential harm to SWBT arises only if such a subsidy is funded through charges that it must pay. Otherwise, SWBT should be indifferent.8 The salient question, therefore, is whether reciprocal compensation rates (paid by either SWBT or CLECs to the other) *provide* a subsidy. It is a well accepted principle of economics that a service can be shown to be the recipient of a subsidy only if generates revenues less than its incremental cost, and provides a subsidy only if it

8 This indifference should work both ways. CLECs should be willing to pay reciprocal compensation for calls originated by their end user customers that are then delivered by SWBT to called party whose service is being subsidized (an residential subscriber in a rural area, for example).

generates revenues in excess of its stand-alone cost. In Texas, the established rates for reciprocal compensation are not above stand-alone cost, and in fact are not above incremental cost. The rates are set at the level adopted as TELRIC-compliant by this Commission. It is difficult to understand how a rate that is cost-based (and in fact is set equal to cost) can be seriously held forth as the source of a subsidy. Dr. Harris' argument may have had merit if the Commission had adopted SWBT's proposal to establish reciprocal compensation rates at a level above cost, or if it had accepted SWBT's original overstatement of the cost of the components of reciprocal compensation. Neither of these outcomes took place, however. Instead, the Commission adopted reciprocal compensation rates equal to cost. Such rates cannot, by definition, provide the funding for a subsidy.

Dr. Harris goes on in his testimony to advocate the application of the principle of cost causation to the issues in this proceeding. At this level, I agree with his testimony: cost casuation is at the heart of the issue. Dr. Harris then goes on (for example at pages 6 and 9-15) to construct a novel theory regarding the identity of the cost causer. This theory (and its selective application) are illustrated in Table 1 in his testimony. For a local voice call originated by a customer of LEC A and delivered to a customer of LEC B, Dr. Harris apparently agrees that LEC B has been impacted in a way that would result in the payment of reciprocal compensation from LEC A to LEC B. In this scenario, he properly identifies the cost causer as the customer of LEC A who originates the call (Dr. Harris makes no reference to a local data call, but I can only assume that the same treatment would apply). In other words, when the called party is an entity other than an ISP, Dr. Harris correctly identifies the cost causer – the calling party. When an otherwise

identical call is delivered to an ISP as the called party, Dr. Harris asserts that the originating caller (and the LEC that provides it service) is now off the hook, and that the ISP becomes the cost causer. This transformation occurs, according to Dr. Harris, because the ISP is providing the originating caller a service which is accessed via a telephone call. What is strikingly absent from this analysis is the consideration of all other entities who provide a service to consumers that is accessed by a telephone call. According to this logic, calls to banks, brokerage firms, government agencies, restaurant takeout services, and the local psychic hotline should all be exempted from reciprocal compensation.

There is no dispute that ISPs are "attractive" destinations for calls, or that they receive a greater than average number of incoming calls. But as the Court correctly pointed out, there has been no demonstration to date that ISPs are fundamentally different, for the purposes of reciprocal compensation, than any other "communications-intensive business end user selling a product to other consumer and business end users." From the standpoint of the reciprocal compensation-related costs incurred by what Dr. Harris refers to as LEC B, the identity of the called party as an ISP makes no difference whatsoever. The shortcomings of the SWBT position are readily apparent: not only have they not demonstrated that an ISP is fundamentally different from another communications-intensive business, they have not demonstrated that ISPs are fundamentally different from the residence of the local homecoming queen. Simply being an attractive destination for people to call, and/or receiving a greater than average number of calls, does not magically transform the called party into a cost causer.

The inescapable facts remain the following: end user customers of SWBT are making the decision to pick up the phone and dial a seven or ten digit number that will provide them with a connection to the called party of their choosing. Sometimes that called party is the customer of a CLEC, and the CLEC receives the call from SWBT, delivers it to the called party, and incurs the cost of doing so. There is no dispute that the SWBT customer may make the call in order to receive a service from the called party (a bank transaction, a stock trade, a horoscope, or access to information found on the Internet). The fact that a called party is providing a service to the calling party does not mean that the calling party's free will has somehow been subverted, however. The costs in question are created when a call is made that requires collaboration between LECs for its completion. There is simply no way for the called party to initiate such a call, and no way for the called party to cause the cost to be incurred.

Q. IN YOUR DIRECT TESTIMONY, YOU ARGUED THAT THE RESULTS OF THE SWBT-IBT STUDY PROVIDE NO USEFUL INFORMATION TO THE COMMISSION. HAS THE TESTIMONY OF THE SWBT WITNESSES CHANGED YOUR CONCLUSIONS IN THIS REGARD?

A. No. In particular, the testimony of Ms. Smith and Dr. Taylor has reinforced my concerns.

In my direct testimony, I listed two categories of problems with the SWBT-IBT study, either of which would render its results meaningless for the task at hand. First, the study is conceptually flawed; the methodology used is certainly not TELRIC (as the study is labeled) and in fact is not a valid costing methodology at all. Second, the study is a

juxtaposition of data from different (potentially conflicting) sources that ultimately yield costs that are not applicable to either SWBT or CLECs.

While the SWBT-IBT violates several TELRIC principles (and the corresponding FCC rules), two of these violations are certain to have a significant impact on the results. First, the stated cost object of the study – the delivery of calls to ISPs by CLECs – is not a network element, and cannot, by definition, be the cost object of a TELRIC study. Dr. Taylor confirms this at pages 11-12 of his deposition: "So the increment of demand is the supply of the element, calculate the costs associated with that change in supply, look at the number of units of the element, divide one by the other and you get a TELRIC."

The second significant violation is that the SWBT-IBT fails to study the total quantity of the element being studied. Dr. Taylor also verifies (p. 14) the application of this total demand assumption (the "T" in TELRIC): "the demand in question is the total demand for the element, including implicitly both retail and wholesale use of the element. So if it's talking about loops, the volume of demand that's used in calculating TELRIC is all loops, not just the loops that might be sold to CLECs, for example." Dr. Taylor's recollection of the FCC rules is almost right; in fact rule 51.511 explicitly states that the total quantity from both wholesale and retail use of a given element must be included. What SWBT has done when designing the SWBT-IBT study is exactly what Dr. Taylor agrees that it could not do in a TELRIC study: it has studied less than the total quantity of the elements associated with reciprocal compensation, and has in fact studied a subset of the total quantity associated only with the delivery of traffic by CLEC to an ISP. This logical error is identical to the one in Dr. Taylor's example, in which he stated that the

total demand for loops in a TELRIC study could not be "just the loops that might be sold to CLECs."

The reason for the total quantity requirement, as Dr. Taylor correctly points out (pp.15-16), is that "the FCC wanted to be sure that all economies of scale that the ILEC would realize would be included in the price that people who bought these elements would pay." Dr. Taylor also confirms the point made in my direct testimony that the use of less that a total demand assumption (as in the SWBT-IBT) will impact results in an unpredictable way (this unpredictability makes after-the-fact "corrections" to such a cost study difficult or impossible). At pages 21-22, he states that "you can't tell a priori which way using less than the total supply would bias the answer, if it would at all. What that depends upon is how marginal cost s the cost of an additional increment changes with the level of output...If marginal cost varies with the level of output, if it gets higher or lower as output increases, then the numbers would differ, but it depends upon whether marginal cost is increasing or decreasing with output as to whether the TELRIC that you calculated from some subset of the total quantity of demand were greater than or less than the TELRIC that you would calculate if you had used all of the demand. The design of the SWBT-IBT creates just such a problem. The Commission cannot know whether the use of a less than total quantity of demand has biased the results of the study upward or downward. Either way, their reliability is diminished. At pages 20-21, Dr. Taylor also agreed that it would not be appropriate to conduct a TELRIC study by considering only the quantity of the element used to provide service to a given class of customers. The SWBT-IBT does just that: it attempts to calculate the TELRIC of the elements of

reciprocal compensation by studying only that portion of those elements associated with a specific customer class.

Q. WHAT, IN ECONOMIC OR COST METHODOLOGY TERMS, DO THE RESULTS OF THE SWBT-IBT CONCEPTUALLY REPRESENT?

A. Nothing.

Q. YOU ALSO STATED THAT THE SWBT-IBT SUFERS FROM PROBLEMS RELATED TO DESIGN AND IMPLEMENTATION. PLEASE EXPLAIN HOW THE TESTIMONY OF SWBT WITNESSES HAS IMPACTED YOUR CONCLUSIONS IN THIS REGARD.

A. Ms. Smith, in her deposition, makes several statements that underscore my concerns regarding how the SWBT-IBT was conducted. One of the underlying assumptions in the SWBT-IBT study is that SWBT has been able to accurately identify traffic delivered to ISPs. The application of this assumption in the study provides an illustrative example of the poor costing practices used by SWBT when conducting this study. When collecting data from multiple sources to be used in a study of this type, it is important to (1) ensure that the collection methods (in this case selection criteria) are consistently applied to each data source, and (2) the collection method should be thoroughly evaluated before use to ensure that it will yield the most accurate input data possible.

Ms. Smith, the sponsor of the SWBT-IBT, has made it clear that she has done neither of these tasks. The SWBT-IBT utilizes input data from two sources that separately identify ISPs as the end user to which a call is delivered. The ISP Usage Study

(Tab 8 of the SWBT-IBT) is used to determine total "ISP-bound" traffic and the average length of "ISP-bound" calls. The ISP Sample Study, developed through a completely independent process, was used to develop the average busy minutes and messages associated with "ISP-bound" calls. The SWBT-IBT then combines the data from these two sources in a way that assumes that it has been collected in a consistent way (in the simplest terms, it assumes it has apples to combine with apples). In reality, however, the ISP Usage Study and the ISP Sample Study rely on different methods for "identifying" (in reality, guessing at) which end users are ISPs. Undeterred, SWBT has forced the data together in the study.

What is more troubling to me as a cost analyst is that as the sponsor of the SWBT-IBT, Ms. Smith had not examined the methods of data collection used by two important components of her study. She states (pp. 42-54) that while she relied on the results of the ISP Sample Study, she does not know how the two sample offices were selected (or whether they are representative of other offices), how the time period for data collection was selected (or whether it was representative of other time periods), or how the traffic bound for ISPs had been "identified." She specifically had not examined whether the selection criteria for identifying ISPs was the same in the ISP Usage Study and the ISP Sample Study, even though the available information strongly suggested that they were in fact different and therefore potentially inconsistent.

As a cost analyst, I would have reservations sponsoring a study that relied on data from independent sources that, if my results were to be reliable, would have to be consistent. I would not sponsor such a study if I had not evaluated the data collection methods individually for reasonableness and had not attempted to determine if the

approaches were consistent. Ms. Smith apparently has no such trepidation. At pages 60-67, she states that she does not know which methods were used for each data collection effort, does not know how she would evaluate different methods in order to determine which to use, and that she is not bothered by the possibility of inconsistent data sources. When asked, as the sponsor of the SWBT-IBT, whether it troubled her that she didn't know whether data sources underlying her study were consistent, she replied that she had "no opinion on that." If the Commission is being asked to rely on the results of a cost study, it deserves for the sponsor of the study to have an opinion regarding possibility that an important set of inputs to the study (a key factor in the reliability of the results) is in fact invalid.

Q. IN HIS TESTIMONY, SWBT WITNESS LONG SETS FORTH A THREE-PART TEST TO BE APPLIED WHEN DETERMINING WHETHER TANDEM LEVEL RATES SHOULD BE APPLIED. DO YOU AGREE WITH HIS PROPOSAL?

A. No. Mr. Long sets forth a series of arguments in an attempt to support a requirement that in order to receive truly mutual and reciprocal compensation, a CLEC must duplicate the architecture of SWBT's network, including its outdated switching hierarchy. There is no basis for such a requirement in either the FCC rules or sound economics. The development of competition for local exchange service will not be promoted if CLECs are penalized for being more efficient, or if SWBT is rewarded for being less efficient. The reciprocal compensation rate should encourage all LECs to make efficient network deployment decisions.

Mr. Long appears to agree with the FCC's conclusion that "[w]here the interconnecting carrier's switch9 serves a geographic area comparable to that served by the incumbent LEC's tandem switch the appropriate proxy for the interconnecting carrier's additional costs is the LEC tandem interconnection rate." The FCC is clear that in order to provide a capability equivalent to that provided at the ILEC tandem – the ability to have calls delivered throughout the geographic area served by that tandem -- a CLEC need not duplicate the ILEC network design. Instead, the CLEC can provide this equivalent capability by utilizing a more efficient network design, and will not be penalized for doing so.

Mr. Long does not appear to oppose outright the deployment of a CLEC network that is based on a different design theory that SWBTs (one that does not provide geographic coverage through a physically separated switching hierarchy, but instead provides the geographic coverage with a single switch combined with other facilities, for example). This position is consistent with the conclusion of the FCC, cited by Mr. Long, that CLECs need not deploy multiple switches within a given area in order to receive reciprocal compensation. Inexplicably, Mr. Long goes on to argue that while CLECs need not duplicate the inefficient ILEC network design in order to provide comparable geographic coverage, they must nevertheless do so in order to provide comparable "functionality." There is no basis for such a requirement.

Mr. Long hangs his argument on a sentence from paragraph 1090 of the First Report and Order: "states shall also consider whether new technologies (e.g. fiber ring or

9 It is instructive to note that the FCC refers to the CLEC's "switch" rather than to a CLEC's "end office" or "tandem office" throughout the First report and Order and associated section 51 rules. In doing so, the FCC refers to the CLEC's switching capability without assuming the existing ILEC switching hierarchy. The FCC makes

wireless networks) perform functions *similar* to those performed by an incumbent carrier's tandem switch" (emphasis added). Mr. Long's reliance on this language puts him on shaky ground for three reasons.

First, while the cited language refers to "functions similar to those performed by an incumbent carrier's switch, Mr. Long puts forth a proposed requirement (p. 20) that "the CLEC proves that its switch performs the *same functions* on behalf of SWBT that SWBT's tandem switch performs." While Mr. Long would have the Commission believe otherwise, the words "similar" and "same" are not interchangeable.

Second, it is clear from the context of the above-cited sentence that the FCC did not intend the word "functions" to have the meaning that Mr. Long suggests. Through interconnection, CLEC's perform an essential functionality for SWBT: the ability, from a single point of interconnection, to have calls delivered to any point within a geographic area comparable to the area served by SWBT's own tandem. There is nothing in the FCC's language that even remotely suggests that it intended to require CLECs to deploy the essential elements of that functionality by using the same equipment as the ILECs; in fact the opposite is true. A CLEC must, though a combination of network facilities (including but not limited to switches and fiber rings) create the ability for SWBT to have calls originated by its customers delivered to the called party within the geographic area in question. There is no requirement, or even the suggestion of a requirement, that the CLEC provide through its switch a set of functions identical to those that SWBT provides through its tandem.

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reference to end offices and tandems only in the context of the ILEC networks.

Third, and most importantly, it is important to recall that where the legislative intent is unclear, it is OK to look at the plain language of the law. In this case, the applicable FCC rule is clear and requires no further explanation from the language in the Order: [w]here the switch of a carrier other than an incumbent LEC serves a geographic area comparable to the area served by the incumbent LEC's tandem switch, the appropriate rate for the carrier other than the incumbent LEC is the incumbent LEC's interconnection rate" (Rule 51.711 (a) (3)). This rule makes it clear that in order for a CLEC to receive the tandem level interconnection rate, it need only provide to the ILEC the following "functionality": the ability to have calls delivered to a geographic area "comparable to the area served by the incumbent LEC's tandem switch." The CLEC need not make that functionality available in the same manner as the ILEC, either by deploying the same switching hierarchy or by providing the elements of this functionality by using the same equipment as the ILEC.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

ATTACHMENT D

BEFORE THE

PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking on the Commission's Own Motion into reciprocal compensation for telephone traffic transmitted to Internet Services Providers modems.	**R.00-02-005**

Direct Testimony

and

Exhibit

of

LEE L. SELWYN

on behalf of

Pac-West Telecomm, Inc.

July 18, 2000

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Because ISPs are end users of telecommunications services and are not telecommunications service providers, the compensation arrangements applied to interexchange carriers (IXCs) should not be applied to ISPs. 16

Under the sent-paid framework, explicit reciprocal compensation payments must be made for call termination when traffic flows are significantly out of balance. 23

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Internet Services Provider (ISP)-bound traffic is technically indistinguishable from other in-bound data and voice local traffic, and should not be singled out for discriminatory treatment with respect to how CLCs are compensated for terminating such traffic. 31

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While CLC networks tend to employ a different mix of facilities than ILEC networks, they provide the same functionality for local telecommunications traffic (including ISP-bound calls) as do ILEC networks, including the interexchange carriage of traffic performed by ILECs' tandem switches and shared transport. 43

The appropriate inter-carrier compensation for the termination and transport of ISP-bound local calls, as well as other forms of local traffic, is a symmetric rate based upon the ILEC's prevailing TELRIC cost level, which creates incentives for continual reductions in the costs of call termination services and harms neither ILECs nor end users. 52

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INTRODUCTION

Qualifications

Q. Please state your name, position and business address.

A. My name is Lee L. Selwyn; I am President of Economics and Technology, Inc. ("ETI"), One Washington Mall, Boston, Massachusetts 02108. Economics and Technology, Inc. is a research and consulting firm specializing in telecommunications economics, regulation, management and public policy.

Q. Please summarize your educational background and previous experience in the field of telecommunications regulation and policy.

A. I have prepared a Statement of Qualifications, which is attached hereto as Attachment 1.

Q. Have you previously testified before the California Public Utilities Commission ("commission")?

A. I have participated in numerous other proceedings before the Commission dating back to the mid-1970s; these appearances are also summarized in Attachment 1.

Assignment

Q. By whom were you engaged, and what was your assignment in this proceeding?

A. ETI has been engaged by Pac-West Telecomm, Inc. (Pac-West), to provide expert assistance and analysis with respect to the issues considered in this proceeding. Relative to this direct testimony, Pac-West requested that I undertake an economic and policy analysis of the Factual Issues identified in the Assigned Commissioner's Ruling of May 2, 2000 and prepare testimony responsive to the Commissioner's request for evidence on those issues.

Summary of Testimony

Q. Please summarize the testimony you are presenting at this time.

A. The first section of my testimony ("Inter-carrier Compensation for Internet-Bound Traffic") responds to Factual Issues 5-10 (exclusive of Issue 8, which has been deferred) of the Assigned Commissioner's Ruling. In order to reach a proper understanding of the financial implications of ISP-bound traffic for ILECs, CLCs, and their customers, one must first take into account the existing compensation arrangements applied to traditional telecommunications traffic. My testimony explains that local telephone calls in California and elsewhere in the US are nearly always undertaken on a "sent-paid" basis, meaning that the customer who originates the call pays his or her local carrier to get the local call from the point of origin all the way to its intended destination. Most importantly for the purposes of this proceeding, under the "sent-paid" framework, the costs of terminating the call are paid in full by the call originator (to the carrier that originates the call), so that the recipient of the

call need not and should not make any additional payments for the termination of that call. When two interconnecting carriers jointly complete a local call, the originating carrier is responsible for remitting a portion of the sent-paid revenue to the carrier that terminates the call. Reciprocal compensation is simply the payments made by the first (originating) carrier to the second (terminating) carrier for its work in completing the call. Despite ILEC arguments to the contrary, there is no compelling economic or policy basis to deviate from the traditional "sent-paid" framework and reciprocal compensation obligations in the case of ISP-bound traffic. Some ILECs have contended that heavy use of dial-up ISP services has been driving up their average per-line local usage and associated costs, but in fact, ILECs have enjoyed strong growth in residential second lines so that the average volume of local usage per line has not materially increased.

The major alternative to the "sent-paid" approach to inter-carrier compensation is the access charge framework applied to interLATA toll calls. Some ILECs and ILEC-sponsored economists have argued that ISPs are functionally equivalent to interexchange carriers, and urged regulators to allow ILECs to adopt the access charge framework to ISP-bound calls as a substitute for the "sent-paid" framework. However, as the D.C. Circuit Court of Appeals confirmed earlier this year, ISPs are users of telecommunications services, not telecommunications providers like interexchange carriers, and therefore should not be treated any differently in this respect from other businesses subscribing to telephone services. ILEC arguments that an access charge regime is justified by an analysis of cost-causation for ISP-bound calls are equally without merit. Furthermore, if ILECs were allowed to apply their existing instrastate switched access charges to ISP traffic, Internet users would be exposed to potentially vast increases in the rates they pay for dial-up connection to ISPs, as much as $15.14 per month in Pacific Bell's California service

territory.

Under the sent-paid framework, when the exchange of traffic between two carriers is roughly equal, carriers may elect a "bill and keep" system, thereby eliminating the need for explicit inter-carrier payments. However, explicit reciprocal compensation payments must be made for call termination when inter-carrier traffic flows are significantly out of balance, in order to ensure that each carrier is properly compensated for the termination work that it performs.

In California and elsewhere, the ILECs' ability to effectively dictate reciprocal compensation rates in their negotiations with CLCs meant that CLCs faced call termination rates significantly higher than they had originally proposed. As a result, many CLCs have pursued the market for call termination services needed by ISPs and other businesses with high volumes of inbound traffic, frequently leading to unbalanced one-way traffic flows with interconnecting ILECs. However, under a system of explicit reciprocal compensation payments and as long as the ILEC's rates are based upon the ILEC's costs, there is no logical connection between the traffic flow and associated compensation due in one direction, and the traffic flow and compensation that might occur in the reverse direction. Assuming that ISP-bound calls are subject to reciprocal compensation at all, then in each direction, compensation must be paid for the work performed by the terminating carrier C and thus, the volume of traffic that may or may not flow in the reverse direction is irrelevant.

The second section of my testimony ("Economic and Technical Characteristics of ISP-bound Calls and Other Concentrated Inbound traffic") responds to Factual Issues 1-4 of the Assigned Commissioner's Ruling. Some ILECs have contended that reciprocal compensation arrangements with CLCs should make a distinction between traffic that is

destined for (terminated at) a conventional voice telephone line, and traffic that is terminated to an ISP. In fact, there is no technical difference in the manner by which these two types of traffic are handled in the ILEC's network and by suggesting otherwise, such ILECs are attempting to introduce a market-driven price discrimination based upon the use to which local telephone service is put rather than on the processes by which it is produced or the costs incurred in its production. My testimony explains why such an attempt to create a distinction between "ordinary" and ISP-bound traffic is without economic or technical merit and should be rejected by this Commission. In fact, it is a sheer impossibility for ILECs to accurately identify ISP-bound calls even if a discriminatory pricing regime were to be adopted.

My testimony also describes and compares the architecture and design of ILEC networks vis-a-vis CLC networks, and explains why a CLC should be considered to be providing the same traffic aggregation function as occurs via an ILEC's tandem switching, despite the fact that the design of CLCs' local networks differs from that used by ILECs such as Pacific. Indeed, not only do CLCs confront costs that are no lower than those of an ILEC, it is reasonable to expect that the significant differences in the structure of these networks accounts for differences in both the structure and the level of the ILECs' and the CLCs' respective costs of processing and terminating local calls. In fact, ILECs including Pacific have submitted studies to the FCC that claim that the concentrated nature of ISP-bound traffic has caused them to incur network investments and costs incremental to their ordinary call termination costs – costs that presumably those CLCs specializing in terminating concentrated inbound traffic must also be incurring.

Finally, I explain that the appropriate inter-carrier compensation for the termination and

transport of ISP-bound local calls, as well as other forms of local traffic, is a symmetric rate based upon the ILEC's prevailing TELRIC cost level, which creates incentives for continual reductions in the costs of call termination services and harms neither ILECs nor end users. These incentives and the positive market developments they engender were expressly recognized by the FCC during its design of the prevailing reciprocal compensation rules for local telecommunications traffic, and are congruent with the regulatory objectives that this Commission articulated during the establishment of the New Regulatory Framework applied to Pacific and GTEC.

INTER-CARRIER COMPENSATION FOR INTERNET-BOUND TRAFFIC[1]

A "sent-paid" compensation arrangement has traditionally been applied to local telecommunications traffic, and remains the most rational approach to apply to Internet Services Provider (ISP)-bound traffic that is rated as local and subject to local tariff rates.

Q. Dr. Selwyn, what is the traditional practice in California and across the United States generally for compensating local exchange carriers (LECs) for their carriage of local telephone calls?

A. The almost universal practice in California as well as generally throughout the US is for local calls to be provided on a "sent paid" basis by the local exchange carrier on whose network the call originates. By that I mean that the customer who originates the call pays his or her local carrier to get the local call from the point of origin all the way to its intended destination, which means that the originating carrier is compensated by its customer for local switching at both the originating and terminating ends of the call as well as for transporting the call the entire distance between the originating switch and the terminating switch. Most importantly in the context of this proceeding, the "sent paid" approach means that the calling party pays in full for the *termination* of the call, as well as for its origination, *even if a carrier other than the originating (and billing) carrier ultimately terminates the call.*

The "sent paid" payment arrangements can take many forms, including flat-rated local calling over a wide area; "extended area service" or "extended area calling" plans that have

1. This section of my testimony responds to Factual Issues 5-10 as set forth in the May 2, 2000 Assigned Commissioner's Ruling. However, I do not address Factual Issue 8, which was set aside for later consideration in the June 26, 2000 ALJ's Ruling Granting Motion for (continued...)

the same effect; flat-rated local calling over a smaller area with some type of message unit or local measured charge for local calls outside that area; flat-rated local calling for a certain number of calls per month, with a per-message or other charge for usage above that level; and even local service with no usage included in the base price at all, with each call subject to a separate local message unit or measured service charge.

Q. Is the "sent paid" approach used in California today?

A. Yes, it is. In California, both Pacific Bell and GTEC offer local usage services under a combination of flat and measured rate elements, but in all cases the charges for these services are paid by the customer who originates calls. For example, Pacific's residence customers generally obtain local service under the Company's tariffs for flat-rate or measured rate exchange service. Pacific's Individual Line Flat-Rate Residence Service provides for unlimited outward calling within a defined local calling area, which consists of the customer's home and certain nearby exchanges.[2] Residence customers may alternatively choose Pacific's Individual Line Measured Rate Residence Service where, for a lower monthly charge than that which applies for flat-rate local service, the customer receives a $3.00 monthly "allowance" of outgoing local messages,[3] and is then charged usage-sensitive rates for each originated call in excess of that allowance.[4]

Pacific's business customers may subscribe to Individual Line Business Measured Rate

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Clarification.

2. See Pacific Bell Schedule CAL P.U.C. A5.
3. Pacific Bell Schedule CAL P.U.C. A5, Sheet 235 (revision 6), Effective November 1, 1999.
4. Pacific Bell Schedule CAL P.U.C. A5, Sheet 234 (revision 7), Effective November 1, 1999.

Service under Pacific's local exchange tariff, which does not provide any usage allowance for outgoing local messages.[5] Pacific does not offer a flat-rate local exchange tariff to business customers in California.

In some communities, Pacific's local service customers are required to subscribe to mandatory "Expanded Area Service" (EAS), in which one or more additional exchanges are included in the customer's local calling area (where no long distance charges apply) for an additional fixed rate increment which is folded into the applicable monthly exchange rate for that exchange. (Calls placed to all other points within the same LATA are rated as intraLATA toll.) In the principal metropolitan areas of the state, flat- or local measured-rate calling is limited to an area within twelve (12) "rate miles"[6] of the exchange from which the call is originated. Calls in excess of 12 miles and up to 16 miles are rated as "Zone Usage Measurement" ("ZUM") calls that are considered "local" for jurisdictional purposes and are included within the monthly calling allowance for measured-rate residence service (whereas intraLATA toll charges are not), but which carry toll-like per-minute charges that are higher than the rates applicable for calls within the 12-mile band. Whatever the precise form of local service plan, and whether priced on a flat-rate or usage-sensitive basis, what is common to all of them is that the *originating end user* pays the *originating local carrier* an amount designed to cover the entire cost of getting the call from the origin to its destination.

5. Pacific Bell Schedule CAL P.U.C. A5, Sheet 210.2 (revision 1), Effective March 10, 1998.

6. Distance for call rating purposes is calculated from the basing point of the originating exchange to the basing point of the terminating exchange, using so-called Vertical and Horizontal (V&H) coordinates as specified in National Exchange Carrier Association (NECA) Tariff No. 4. Actual distances from the calling to the called parties' locations may vary, up or down, from these "rate mile" calculations.